



KANSAS

DIVISION OF THE BUDGET
DUANE A. GOOSSEN, DIRECTOR

KATHLEEN SEBELIUS, GOVERNOR

April 25, 2005

To: Governor Kathleen Sebelius and the Legislative Budget Committee

From: The Kansas Division of the Budget and the Kansas Legislative Research Department

Re: State General Fund Receipts for FY 2005 (Revised) and FY 2006 (Revised)

Estimates for the State General Fund are developed using a consensus process that involves the Division of the Budget, the Legislative Research Department, the Department of Revenue, and three consulting economists from state universities. This estimate is the base from which the Governor and the Legislature build the annual budget. The Consensus Group met on April 18, 2005, to revise the FY 2005 and FY 2006 estimates.

For FY 2005, the estimate was increased by \$55.0 million, or 1.2 percent, above the previous estimate, which was made in November 2004. The overall revised SGF estimate of \$4.686 billion is 3.7 percent above actual FY 2004 receipts. The estimate for FY 2006 was increased by \$20.2 million, or 0.4 percent, above the previous estimate, which was made also in November 2004. The initial FY 2006 estimate did not subtract any demand transfers which have been converted to revenue transfers. However, the revised FY 2006 estimate subtracts \$74.9 million in these transfers because the action is now law. If transfers had been treated in a similar fashion in both the November and April estimates, the FY 2006 increase would have been 1.4 percent. The total additional increase in tax receipts for both fiscal years is \$127.4 million.

Detailed information regarding the specific sources of revenue constituting total receipts is presented in Table 1. Table 2 and Table 3 compare the FY 2005 and FY 2006 estimates developed last November with the recently revised estimates. Table 3a reflects the FY 2006 estimates when revenue transfers are treated in a similar fashion.

Economic Forecast for Kansas

The Kansas economy is expected to continue the trend of positive growth, although moderating through calendar year 2006. Several key factors that affected the consensus estimates include high energy prices; the changing outlook for the stock market; inflation concerns; a steady unemployment rate; an improved agricultural sector; and steady retail sales.

The national economy is expected to grow at a slower pace over the next two years. Nominal Gross Domestic Product (GDP) is expected to grow by 5.7 percent in 2005; and by 4.9 percent in 2006, while real GDP is expected to grow by 3.7 percent, and 3.1 percent. U.S. nominal personal income is expected to decrease. The growth is anticipated to be 5.7 percent in 2005; and 5.6 in 2006. A listing of the key economic indicators is shown in the following table:

Key Economic Indicators

	2003	2004	2005	2006
Consumer Price Index for All Urban Consumers	2.3 %	2.7 %	2.4 %	2.2 %
Real U.S. Gross Domestic Product	3.0	4.4	3.7	3.1
Nominal U.S. Gross Domestic Product	4.9	6.6	5.7	4.9
Nominal U.S. Personal Income	3.2	5.6	5.7	5.6
Corporate Profits before Taxes	15.0	12.6	35.0	--
Nominal Kansas Gross State Product	4.5	5.8	4.9	4.6
Nominal Kansas Personal Income:				
Dollars in millions	\$80,466	\$84,282	\$88,900	\$93,400
Percentage Change		5.1 %	4.5 %	5.1 %
Nominal Kansas Disposable Income:				
Dollars in millions	\$72,451	\$76,004	\$79,400	\$82,700
Percentage Change		5.3 %	4.5 %	4.2 %
Interest Rate for State General Fund (based on fiscal year)	1.63	1.19	1.63	3.82
Kansas Unemployment Rate (based on fiscal year)	5.3	5.7	5.4	5.5

Inflation Rate

In 2004, the rate of inflation, as measured by the Consumer Price Index for All Urban Consumers (CPI-U), was 2.7 percent. The inflation rate in 2005 is expected to be lower at 2.4 percent. The rate is anticipated to decline further to 2.2 percent in 2006.

Kansas Personal Income

Kansas Personal Income (KPI) is expected to grow by 4.5 percent in 2005. The growth rate is expected to increase to 5.1 percent in 2006.

Interest Rates

The Pooled Money Investment Board is authorized to make investments in U.S. Treasury and agency securities; highly rated commercial paper; and repurchase agreements and certificates of deposit of Kansas banks. In FY 2004, the state earned 1.19 percent on its State General Fund portfolio. The average rate of return forecasted for FY 2005 is 1.63 percent. For FY 2006, the forecasted rate is 3.82 percent.

Employment

The Kansas Department of Labor stated that the U.S. Department of Labor made a significant change to its methodology in early 2005. The Kansas Department of Labor anticipates that the change in the way that the unemployment rate is calculated has translated into a slightly higher unemployment rate. Adjustments will be made back to 2000, when the last decennial census was conducted.

Newly revised labor market statistics indicate that unemployment in Kansas is down, and experts believe that the employment outlook generally is improving. The statewide unemployment rate for FY 2004 was 5.7 percent and is expected to drop to 5.4 percent in FY 2005 and then increase slightly to 5.5 percent in FY 2006. The latest statistics indicate that Kansas unemployment is slightly above the national rate of 5.2 percent (March 2005).

Agriculture

The All Farm Products Index of Prices received by Kansas farmers was 111 in March, which was up 4 points from February, but down 3 points compared with a year ago. Prices for wheat, corn, sorghum, and soybeans were up from February, but much lower than March 2004 levels. Wheat prices in mid-March, at \$3.40 per bushel, were up \$0.14 from February, but \$0.33 below last March. Corn prices, at \$2.05 per bushel, were up \$0.15 from February, but \$0.87 below last March. Farmers received an average of \$3.09 per cwt for sorghum grain, which is \$0.22 cents higher than February, but \$1.60 below last March. Soybean prices, at \$6.02 per bushel, were up \$0.81 from February, but \$3.32 below last March.

Beef cattle and hog prices are higher than February's levels, as well as last year's levels. All beef cattle brought an average of \$90.40 per cwt in mid-March, which is up \$2.50 from February and \$4.20 above the price last March. The all hog price of \$49.80 per cwt for mid-March was up \$2.20 from February and up \$6.00 from last March.

Oil and Gas

The average price per taxable barrel of Kansas crude oil is estimated to be \$44 in FY 2005 and to remain steady through FY 2006. Gross oil production in Kansas is expected to remain steady at 34.0 million barrels throughout the forecast period (FY 2005 and FY 2006).

The price of natural gas is expected to increase from the FY 2004 level of \$4.17 per mcf to \$5.00 per mcf in FY 2005 and then to \$5.50 per mcf in FY 2006. Natural gas production in FY 2004 was 417.6 million cubic feet. Production is expected to continue to decline for the foreseeable future as natural gas reserves, especially those in the Hugoton field, are depleted. The forecast is for 385.0 million cubic feet in FY 2005 and 355.0 million cubic feet in FY 2006.

State General Fund Receipts Estimates

Each individual SGF revenue source was evaluated independently, and consideration was given to revised and updated economic forecasts and year-to-date receipts. Additional information was provided by the Department of Revenue, the Insurance Department, the State Treasurer's Office, the Pooled Money Investment Board, the Kansas Department of Labor, and Kansas Agricultural Statistics.

Tax Receipts

FY 2005. Estimated tax receipts for FY 2005 were increased by \$55.7 million, or 1.2 percent, while total receipts were increased by \$55.0 million from the November 2004 estimate. Individual income tax receipts account for \$37.0 million of the total increase, while corporation income tax receipts account for another \$18.0 million. One factor supporting the increase in the individual income tax estimate is that during tax year 2004, many individuals who are paid on a biweekly basis received 27 paychecks. The additional withholding taxes from this paycheck translated to an additional \$20.0 million in individual income tax receipts. The remaining \$17.0 million is attributed to growth in Kansas personal income and an increase in the average balance due per tax return. The increase in corporation income tax receipts is attributed to better than expected profits during the last quarter of tax year 2004 and the current economic expansion in business investment.

The retail sales tax estimate was held steady for FY 2005 at \$1,650.0 million, while the compensating use tax estimate was increased by \$9.0 million from \$233.0 million to \$242.0 million. This tax source estimate was affected by an apparent increase in business purchases.

The \$4.2 million decrease to the severance tax estimate is attributable to lower than anticipated prices during the last four months. Experts indicate that the expected price surge in December, January, and February did not occur because it was a warmer than expected winter across the U.S.

Other tax source estimates that were increased include motor carrier property tax, estate tax, and insurance premiums. Motor carrier receipts were increased by \$2.0 million because there are more carriers and operating units that were valued for tax year 2004. The estate tax estimate was increased by \$2.0 million from \$50.0 million to \$52.0 million. Insurance premiums also were increased by \$2.0 million from \$100.0 million to \$102.0 million.

Statutory changes were made to the corporate franchise tax during the 2004 Legislative Session. Beginning January 1, 2005, collection of the corporate franchise tax was transferred from the Secretary of State's Office to the Department of Revenue. This tax is assessed against businesses on the basis of \$1.25 per each \$1,000 of net worth. The Secretary of State's Office will continue to collect a fee, which is assessed to all businesses and non-profit organizations. However, the Department of Revenue is now collecting the tax. The overall estimate for both sources was decreased because of various transitional issues relative to the new law.

Only the financial institutions privilege tax and liquor drink tax were held at the November level. All other tax source estimates were reduced slightly.

FY 2006. Total State General Fund receipts are estimated to be \$4.83 billion in FY 2006, while tax receipts are estimated to be \$4.75 billion. The total receipts are \$20.2 million, or 0.4 percent greater than the November estimate. Tax receipts for FY 2006 are estimated to increase \$71.7 million, or 1.5 percent.

The initial FY 2006 estimate did not subtract any demand transfers converted to revenue transfers. If transfers are treated in a similar fashion in both years, as shown in Table 3a, the FY 2006 growth for total SGF receipts would be \$64.9 million, or 1.4 percent. Modest increases are forecast for the principal SGF tax revenue sources in FY 2006.

Accuracy of Consensus Revenue Estimates

For 30 years, State General Fund revenue estimates for Kansas have been developed using the consensus revenue estimating process. Besides the three state agencies identified on the first page, the economists currently involved in the process are Dr. Joe Sicilian from the University of Kansas, Dr. Ed Olson from Kansas State University, and Dr. John Wong from Wichita State University. Each of those involved in the process prepared independent estimates and met on April 18, 2005, to discuss estimates and come to a consensus for each fiscal year.

The table on page 7 presents estimates compared to actual receipts since FY 1975, the fiscal year for which the current process was initiated. The process involves comparing the adjusted original estimate to actual collections and then the final estimate is compared to actual receipts.

Concluding Comments

Consensus revenue estimates are based on current federal and state laws and their current interpretation. The group will meet again in May to adjust these estimates for legislation that passes during the final days of the 2005 Legislative Session. In November 2005, the group will meet to revise the FY 2006 estimate and formulate the initial estimate for FY 2007. Developments that occur between the April and November meetings will be taken into account at that time.

ACCURACY OF STATE GENERAL FUND ESTIMATES
(Dollars in Thousands)

Fiscal Year	Adjusted Original Estimate*	Adjusted Final Estimate**	Actual Receipts	Difference from:			
				<u>Original Adj. Estimate</u>	<u>Final Adj. Estimate</u>	<u>Original Adj. Estimate</u>	<u>Final Adj. Estimate</u>
				Amount	Percent	Amount	Percent
1975	\$ --	\$ 614.9	\$ 627.6	\$ --	-- %	\$ 12.7	2.1 %
1976	676.3	699.7	701.2	24.9	3.7	1.4	0.2
1977	760.2	760.7	776.5	16.3	2.1	15.8	2.1
1978	830.1	861.2	854.6	24.5	3.0	(6.5)	(0.8)
1979	945.2	1,019.3	1,006.8	61.6	6.5	(12.5)	(1.2)
1980	1,019.3	1,095.9	1,097.8	78.5	7.7	1.9	0.2
1981	1,197.1	1,226.4	1,226.5	29.4	2.5	0.1	--
1982	1,351.3	1,320.0	1,273.0	(78.3)	(5.8)	(47.0)	(3.6)
1983	1,599.2	1,366.9	1,363.6	(235.6)	(14.7)	(3.2)	(0.2)
1984	1,596.7	1,539.0	1,546.9	(49.8)	(3.1)	7.9	0.5
1985	1,697.7	1,679.7	1,658.5	(39.2)	(2.3)	(21.3)	(1.3)
1986	1,731.2	1,666.4	1,641.4	(89.8)	(5.2)	(25.0)	(1.5)
1987	1,903.1	1,764.7	1,778.5	(124.6)	(6.5)	13.8	0.8
1988	1,960.0	2,031.5	2,113.1	153.1	7.8	81.6	4.0
1989	2,007.8	2,206.9	2,228.3	220.5	11.0	21.4	1.0
1990	2,241.2	2,283.3	2,300.5	59.3	2.6	17.2	0.8
1991	2,338.8	2,360.6	2,382.3	43.5	1.9	21.7	0.9
1992	2,478.7	2,454.5	2,465.8	(12.9)	(0.5)	11.3	0.5
1993	2,913.4	2,929.6	2,932.0	18.6	0.6	2.4	0.1
1994	3,040.1	3,126.8	3,175.7	135.6	4.5	48.9	1.6
1995	3,174.4	3,243.9	3,218.8	44.4	1.4	(25.1)	(0.8)
1996	3,428.0	3,409.2	3,448.3	20.3	0.6	39.0	1.1
1997	3,524.8	3,642.4	3,683.8	159.0	4.5	41.4	1.1
1998	3,714.4	3,971.0	4,023.7	309.3	8.3	52.7	1.3
1999	3,844.7	4,051.9	3,978.4	133.7	3.5	(73.4)	(1.8)
2000	4,204.1	4,161.0	4,203.1	(1.0)	--	42.1	1.0
2001	4,420.7	4,408.7	4,415.0	(5.7)	(0.1)	6.4	0.1
2002	4,595.8	4,320.6	4,108.7	(565.6)	(12.1)	(211.7)	(4.9)
2003	4,641.0	4,235.6	4,245.6	(395.4)	(9.3)	9.9	0.2
2004	4,605.5	4,450.5	4,518.7	(86.8)	(1.9)	68.2	1.5

* The adjusted original estimate is the estimate made in November or December prior to the start of the next fiscal year in July and adjusted to account for legislation enacted, if any, which affected receipts to the SGF.

** The final estimate made in March or April is the adjusted original estimate plus or minus changes subsequently made by the Consensus Estimating Group. It also includes the estimated impact of legislation on receipts.

Table 1
Consensus Revenue Estimates for Fiscal Years 2005 and 2006
and FY 2004 Actual Receipts

(Dollars in Thousands)

	FY 2004 (Actual)		FY 2005 (Revised)		FY 2006 (Revised)	
	Amount	Percent Change	Amount	Percent Change	Amount	Percent Change
Property Tax:						
Motor Carrier	\$19,498	24.0 %	\$23,000	18.0 %	\$24,000	4.3 %
Motor Vehicle	1,541		1,400			
Ad Valorem	13,718		500			
Total	\$34,757		\$24,900		\$24,000	
Income Taxes:						
Individual	\$1,888,431	7.9	\$1,997,000	5.7	\$2,085,000	4.4 %
Corporation	141,173	34.2	170,000	20.4	175,000	2.9
Financial Inst.	25,435	(18.3)	22,000	(13.5)	22,000	--
Total	\$2,055,039	8.9 %	\$2,189,000	6.5 %	\$2,282,000	4.2 %
Estate Tax	\$48,064	2.4 %	\$52,000	8.2 %	\$52,000	-- %
Excise Taxes:						
Retail Sales	\$1,612,067	2.8 %	\$1,650,000	2.4 %	\$1,700,000	3.0 %
Compensating Use	214,503	(5.1)	242,000	12.8	250,000	3.3
Cigarette	119,789	(7.3)	117,500	(1.9)	116,500	(0.9)
Tobacco Product	4,797	6.4	4,900	2.1	5,000	2.0
Cereal Malt Beverage	2,165	(4.8)	2,100	(3.0)	2,000	(4.8)
Liquor Gallonage	15,843	7.0	15,500	(2.2)	15,500	--
Liquor Enforcement	40,256	3.7	42,300	5.1	44,000	4.0
Liquor Drink	7,154	4.5	7,500	4.8	7,700	2.7
Corporate Franchise	36,806	18.4	40,000	8.7	40,000	--
Severance	84,639	16.3	101,200	19.6	102,200	1.0
Gas	66,052	17.4	71,700	8.6	72,700	1.4
Oil	18,587	12.6	29,500	58.7	29,500	--
Total	\$2,138,019	2.1 %	\$2,223,000	4.0 %	\$2,282,900	2.7 %
Other Taxes:						
Insurance Premium	\$106,864	13.1 %	\$102,000	(4.6) %	\$104,000	2.0 %
Miscellaneous	4,387	(1.0)	4,300	(2.0)	4,300	--
Total	\$111,251	12.5 %	\$106,300	(4.5) %	\$108,300	1.9 %
Total Taxes	\$4,387,130	5.9 %	\$4,595,200	4.7 %	\$4,749,200	3.4 %
Other Revenues:						
Interest	\$13,870		\$27,000		\$54,000	
Net Transfers	16,721		(4,300)		(43,300)	
Demand to Revenue Transfers	(62,699)		(70,616)		(74,933)	
Other Transfers	79,420		66,316		31,633	
Agency Earnings	101,005		68,000		66,000	
Total Other Revenue	\$131,596	27.0 %	\$90,700	(31.1) %	\$76,700	(15.4) %
Total Receipts	\$4,518,726	6.4 %	\$4,685,900	3.7 %	\$4,825,900	3.0 %